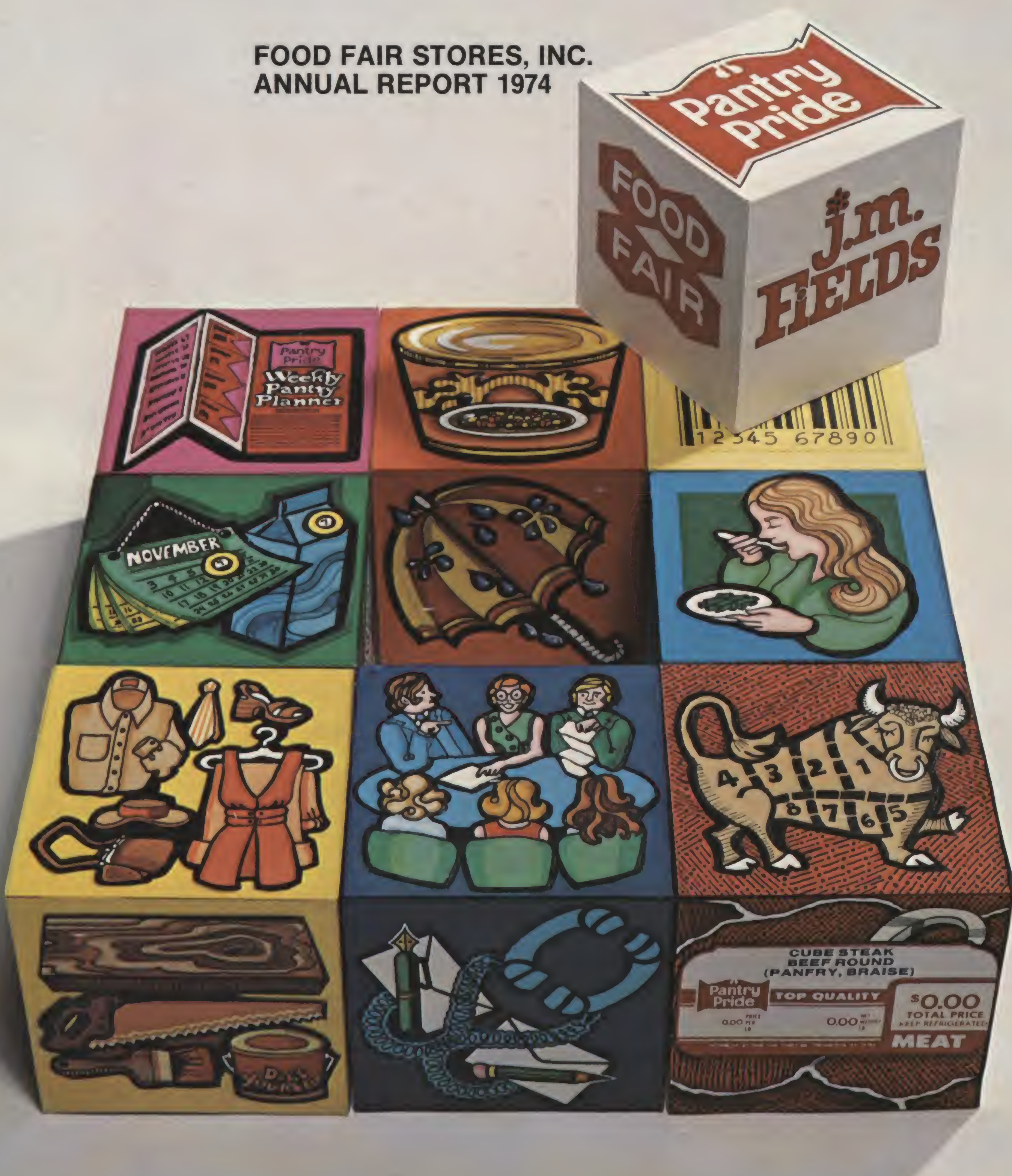
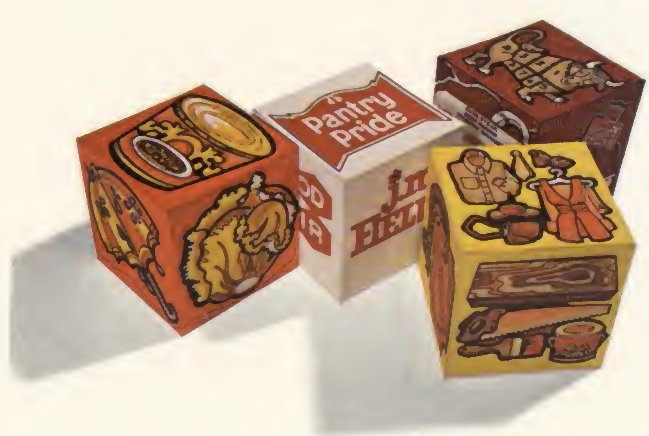
FOOD FAIR STORES, INC.
ANNUAL REPORT 1974



About the Cover . . .

The stylized blocks are representative of the many special programs initiated by the Company in behalf of consumers. These programs reflect the Company's philosophy that consumers will give their loyalty to stores which earn it. Price alone has never been the answer. Shoppers expect honest value, service . . . and more. They will shop where they have confidence . . . where policies of customer satisfaction are clearly spelled out . . . where programs reflect a commitment to and a concern for consumers.



Financial Highlights

	53 Weeks Ended August 3, 1974	52 Weeks Ended July 28, 1973
Sales	**$2,380,561,000**	$2,092,127,000
Income Before Extraordinary Item	**$ 8,926,000**	$ 6,162,000
Provision for Losses Relating to Discontinued Operations		(4,031,000)
Net Income	**$ 8,926,000**	$ 2,131,000
Income Per Share of Common Stock:		
Income Before Extraordinary Item	**$ 1.18**	$ .80
Extraordinary Item		($ .53)
Net Income	**$ 1.18**	$ .27
Cash Dividends	**$ 1,597,000**	$ 1,608,000
Earnings Retained	**$ 7,329,000**	$ 523,000
Current Assets	**$ 305,791,000**	$ 258,306,000
Current Liabilities	**$ 193,943,000**	$ 145,462,000
Shareholders' Equity	**$ 140,208,000**	$ 133,738,000

To Our Shareholders:

We are pleased to report a substantial improvement in earnings and the achievement of record sales for the fiscal year ended August 3, 1974.

Net income rose to $8,926,000, equal to $1.18 a share. This compares with $2,131,000, or 27 cents a share in fiscal 1973, after an extraordinary loss from discontinued operations of $4 million.

Earnings would have shown even further improvement had it not been for the sharp rise in short-term money rates during the year just ended. This was the principal factor contributing to the increase of $4,000,000 in the Company's interest expense, including the interest paid by our credit company, which finances revolving credit and installment sales of J. M. Fields.

Sales increased 13.8% to $2,380,561,000, from $2,092,127,000, continuing the Company's unbroken record of year-to-year sales gains.

The substantial gain in earnings came from our supermarket operations, which have shown steady, consistent recovery from the debilitating price war of 1972 and early 1973.

Aggressive merchandising programs, coupled with stringent cost controls, produced the encouraging results. Consumer response to the discount food merchandising concept of our Pantry Pride and Food Fair Quality/Discount stores was strengthened with the additional conversion of 16 conventional stores to discounting, and the opening of 10 new supermarkets. Twenty-one outmoded units were closed. Thus the higher sales and sharply increased earnings were achieved with fewer units. At year end, there were 470 supermarkets in operation, 11 fewer than at the same time a year ago.

In our general merchandise operations, two new J. M. Fields discount department stores were opened and one older unit was closed.

J. M. Fields, like many general merchandise operations, felt the impact of double-digit inflation which affected consumer discretionary spending. The gasoline shortage early in the fiscal year further aggravated the situation because of our department stores' dependency on drawing shoppers from considerable distances. While sales softened in the wake of these conditions, competition among all general merchandise retailers was intensified as they battled to maintain their volume. At the same time, greater working capital was required for increased costs of inventory. Although this requirement for short-term funds during a period of record-high interest rates affected all of the Company's operations, it was especially burdensome to J. M. Fields. All of these factors created a fiscal year operating loss for the discount department store division.

In prompt response to the situation, a comprehensive review of J. M. Fields operations and merchandising activities was undertaken, leading to a series of actions to generate greater sales and increased operating margins.

While the current state of the nation's economy makes financial predictions somewhat risky, we are reasonably confident that the pattern of improved earnings set in fiscal 1974 will carry through the current year. Our supermarkets are on a firm course of increasing sales and profitability and we believe that the strong measures taken by J. M. Fields will result in improved operations for our general merchandise division. While this last year has been a turbulent one in the general merchandise field, we have confidence in the basic soundness of the low-cost, low-margin discount department store concept. Further, we believe that in a period of economic unrest and consumer uncertainty, the "savings-with-value" appeal of our discount operations will find increased shopper favor.

In planning for the future, your Company took two significant steps during the last fiscal year. In a major corporate structure realignment, a Pantry Pride Supermarket Division has been established for all retail food store operations. This move is part of an overall plan in which the Company's major areas of activities . . . supermarkets, department stores, manufacturing and processing . . . are set up as separate operating divisions for more effective management direction, control and responsiveness to changing conditions.

Also, a corporate long-range planning department has been formed which will concern itself with gathering data and making recommendations to management charting the future growth and profitability of the Company.

Within our corporate officer ranks, Senior Vice President Arthur S. Rosenberg and Vice President Samuel P. Mandell retired during the year. Mr. Rosenberg had served the Company for 35 years in major buying, merchandising and store operations posts. Mr. Mandell, in his 15 years of service, was responsible for produce operations and later for manufacturing operations. Both have made significant contributions to the progress of the Company, for which we are most appreciative. They continue as Directors of the Company.

Leo Dicandilo, formerly an assistant secretary, was elected corporate treasurer. Mr. Dicandilo has been associated with the Company for 16 years in accounting and financial posts. B. F. Lieber, who had served as corporate secretary and treasurer, continues as secretary.

Three other long-service management personnel were elected corporate officers. Leobe Chaimson, director of corporate accounting, and Harvey Richards, controller, have been named assistant secretaries, and Franklin A. Gaber has been named assistant treasurer.

Looking ahead, we are presently testing electronic checkouts in several supermarkets in preparation for the wider introduction of this computer-oriented system which holds excellent promise for improved efficiencies in operation.

In the current fiscal year, we shall open approximately the same number of stores as last year. One of these units, scheduled for early 1975, will be a huge 60,000 square-foot Pantry Pride Discount Center combining all the food items found in a modern supermarket with a wide array of general merchandise including soft goods, apparel, housewares, small appliances, and health and beauty aids. This store will also include a modern pharmacy.

We shall also continue the program of converting our remaining conventional supermarkets to discounting operations. This program which has met with excellent sales success should be completed by year end.

Our major concentration and commitment of capital funds will be to the modernization and enlargement of our existing retailing facilities to enhance their sales and earnings capabilites. In view of the current state of the economy, we believe this to be a prudent short-term course of action.

The current fiscal year, like the one recently ended, will be marked by deep consumer concerns about escalating prices. These concerns are understandable. However, one fact should be borne in mind: While prices for merchandise have climbed as a result of wholesale cost increases over which we have no control, our low price policy has been maintained, despite our own dramatically higher operating costs for labor, utilities, interest, supplies and equipment. We have absorbed much of these costs and continue to do all we can through efficiencies in our operations to soften the inflationary impact on consumers' hard-pressed budgets.

In closing, we wish to extend a special vote of thanks and appreciation to our more than 30,000 employes for their excellent performance, in a year beset with many challenges.

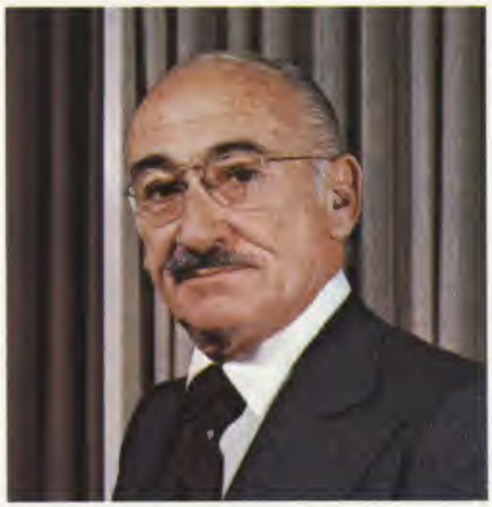
We pledge to them and to you, our shareholders, our continued dedication to the sound, profitable growth of this enterprise in whose successful future we all have a stake.

Sincerely,

Myer B Marcus
Myer B. Marcus
Chairman

Jack Friedland
Jack Friedland
President

October 25, 1974



Myer B. Marcus
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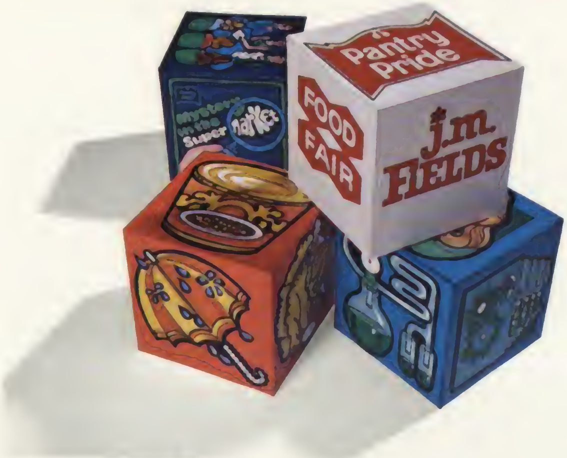

The Year in Review

Supermarket Operations

The major activities of the Company—supermarkets, department stores, manufacturing-processing—have now been grouped into three profit centers with the establishment of the Pantry Pride Supermarket Division for all retail food store operations.

Six Company veterans with many years of buying, merchandising and marketing experience have been promoted to the position of divisional vice president and will serve as the supermarket division staff. They are: Beryl Weinstein—grocery buying and merchandising; Jack Miller—meat, delicatessen and seafood operations; Jack Marcus—produce and baked goods merchandising; Jack Silverman—produce buying and packaging operations; David Epstein—dairy buying and merchandising, and Sheldon B. Sosna—marketing.

Promoted to the post of divisional assistant vice presidents are: Sidney Beck—seafood buying and merchandising; Ronald Stubin—delicatessen buying and merchandising, and Robert Wein—produce buying and packaging.

Seymour I. Friedman, Linden Region manager, was named regional vice president for stores in the northern New Jersey area, with additional responsibility for warehousing and transportation and other support services for stores in New York and Connecticut as well.

Ten new supermarkets were opened during the year and 21 older units were closed, reducing to 470 the number in operation at fiscal year end. Although fewer in number, these stores, 90% of which operate under a discount merchandising program as Pantry Pride and Food Fair Quality/Discount, rang up record sales and substantially improved earnings.

Of the new stores, all in the 30,000 to 35,000 square-foot size, two were opened in Mobile, Alabama, the first for the Company in that state. The others are in our existing market areas.

The program of converting the remaining of our conventional Food Fair supermarkets to discount operations continued unabated. Sixteen stores, most of them in south Florida, were converted in fiscal 1974, and enjoyed substantially increased sales. In addition, six Pantry Pride markets were remodeled and enlarged.

Discount Department Stores

Two new J. M. Fields stores were opened in the fiscal year and one older unit was closed, bringing to 85 the number of stores serving shoppers in 11 states along the eastern seaboard from New Hampshire to Florida. The new stores are in Portsmouth, Virginia, and Margate, Florida.

During the year, Robert M. Hunt, a 25-year veteran, was appointed senior vice president of sales and operations. Mr. Hunt had held the position of senior vice president—operations and store planning.

At the same time, Edward Raskind and Robert Triglia were appointed regional vice presidents, North and South Regions, respectively.

Concurrently, there has been a move to greater decentralization of the operating units in order to better meet the indigenous needs of particular marketing areas. Advertising is more heavily tailored to the requirements of individual stores.

In many stores, a "do-it-yourself" department has been provided with expanded lines of handyman tools and supply items.

The two new stores scheduled for the current fiscal year have already opened in recent weeks, in Utica, New York, and Pottstown, Pennsylvania.

Both of these 100,000 square-foot, one-level, self-service units incorporate major changes in merchandise assortment and display and a totally new interior design concept. Consumer response has been most encouraging.

Recognizing that well-merchandised stores enjoy a real competitive advantage, J. M. Fields merchandise assortments and promotional plans are regularly reviewed and strengthened. However, good merchandising involves not only the replenishment, display and promotion of current assortments, but also the testing of new products, price lines and categories to increase sales. In all of these areas, J. M. Fields is placing greater emphasis.

Manufacturing

The Company began the manufacture of private label instant iced tea mix, non-dairy creamer and instant orange-flavored drink mix in a 6,000 square-foot extension of our tea packaging plant in Philadelphia.

With a return to more favorable market conditions, our Allen Meat Packing Plant in Elizabeth, N.J., resumed operations in the spring. The plant had been closed during the price freeze when it could not be operated profitably. Prior to reopening, the facility underwent extensive remodeling and fixturing, including the installation of the most advanced pollution control equipment.

Allen Packing supplies fresh meat products to wholesalers, restaurants and other institutional buyers.

Distribution Services

A frozen food buying office and warehouse was established in Tampa, Florida, to serve all stores in Florida, Georgia, South Carolina and Alabama. The new operation will effect economies in buying and distribution and replace frozen food warehouses in Miami and Jacksonville.

Backhauling—the use of Company delivery trucks to pick up merchandise from suppliers destined for our warehouses—is proving to be an important tool in reducing freight costs. Backhauling has increased in the Company by nearly 40% over last year.

Energy Conservation

A series of conservation measures were taken during the year in a concerted effort to reduce energy usage at all Company facilities. Lighting was curtailed in all stores and thermostats were turned down. Similar measures were taken at other Company locations.

In meetings with engineers representing manufacturers of refrigerated equipment and officials of utility companies, we are planning energy conservation into the design of new and remodeled stores. This is part of a long-range effort to develop a total environmental package for energy conservation in our stores.

Organization Changes

Organization changes have been effected in our corporate services group. Corporate construction activities have been consolidated into the Tulip Construction Division. Marvin Kushner, national director of facilities, has been named vice president of the Tulip Construction Division.

A separate division has also been established for real estate operations. Sidney Tucker, national director of real estate, has been named vice president of the Tulip Real Estate Division.


PRODUCE
69
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CRISPY
FRUIT PUNCH


Pantry Pride


YOU WIN.
WE DON'T
PLAY GAMES

Commitment To Consumers

Price alone has never been sufficient to earn and hold consumer loyalty. Even in today's inflationary economy, consumers will give their allegiance to those stores in which they "believe" . . . stores in which they can shop with confidence . . . stores which stand behind the merchandise they sell . . . stores whose programs and policies reflect an honest concern for the consumer.

Our supermarkets and department stores have long recognized these basic tenets of merchandising success and have recently undertaken a series of programs to dramatize that fact.

In our supermarket division, a campaign has been mounted, based on extensive consumer research, which has as its theme: At Pantry Pride/Food Fair—"You Win. Because We Don't Play Games." This campaign which points to "games" many consumers feel are played on them by supermarkets—games which are not played by Pantry Pride/Food Fair—has strengthened our reputation for concern for the consumer.

Consumer Affairs Departments have been established in our supermarket and discount department store divisions. In our supermarket division, consumer advisory boards have been organized in many areas. These boards, composed of supermarket shoppers, meet every three months to discuss supermarketing problems from the shopper's point of view.

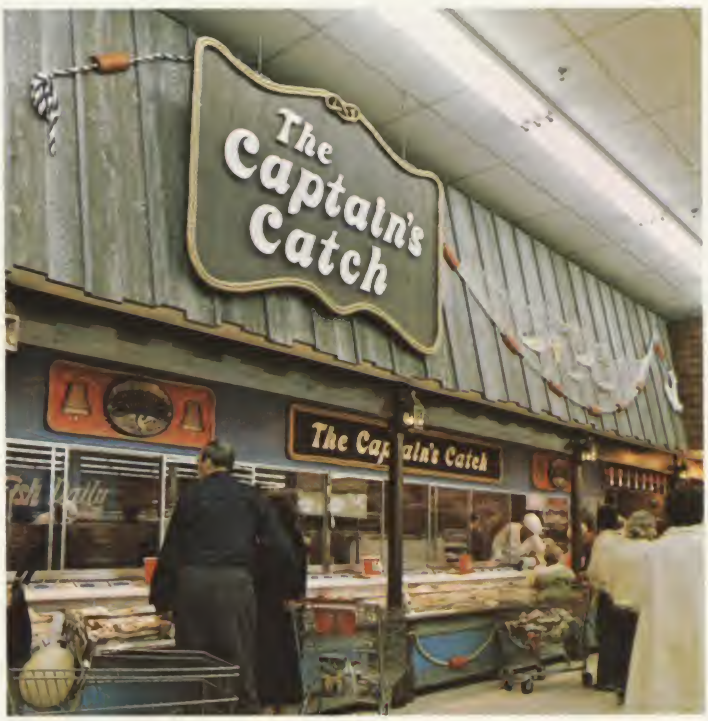
In addition, the supermarket division has adopted "open dating" of products and unit pricing as consumer shopper aids. Open dating provides a clearly stamped and understandable date on the product for freshness control, replacing an undecipherable code. Unit pricing enables consumers to make value comparisons among different brands of the same item, on the basis of cost per ounce or pound or other standard unit of measure.

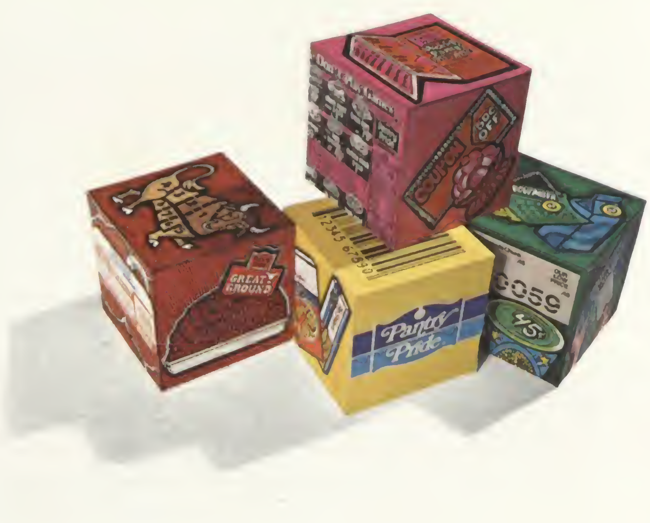
Special Pantry Pride planners issued by the Consumer Affairs Department serve as valuable sources of consumer education, covering subjects like budget-meal planning, nutrition, and food preparation techniques.

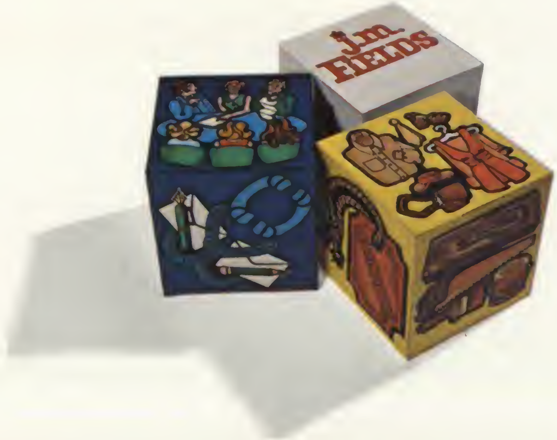
A total redesign of our private labels is in process, which will provide valuable nutritional information for consumers. Included is such information as calories per serving, quantities of protein, carbohydrates and fat, as well as amounts of specified vitamins and minerals, in terms of the new U.S. Recommended Daily Allowances. At the present time, the federal government requires nutritional labeling only if any vitamin, mineral or protein has been added to the product or if nutritional claims are made for it. Nutritional labeling is optional for other food items, but the Company has been including such information on all of its products.

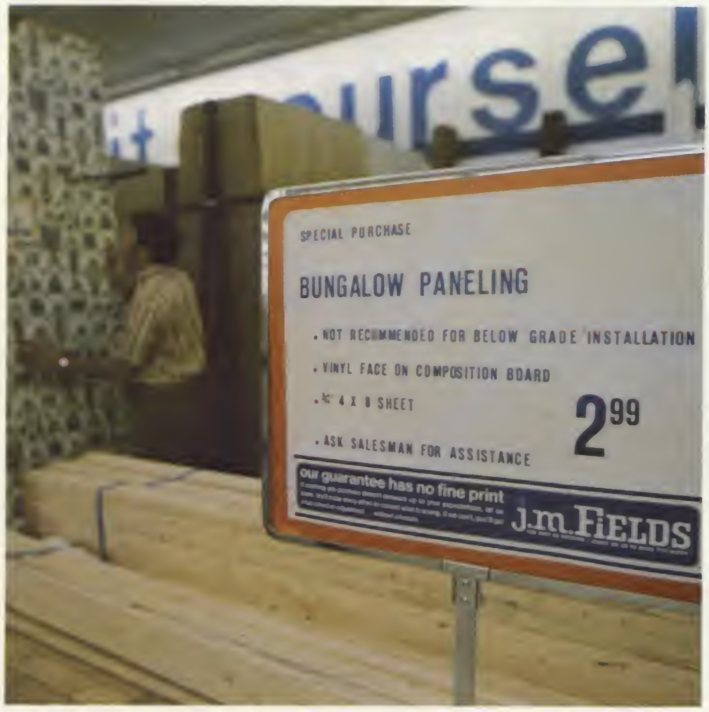
The new labels will also include the Universal Product Code, a grocery product identification system, required for automatic scanning with the introduction of electronic checkouts.

We stand behind the quality of our private label products, and guarantee they must taste as good or better than the national brands. If not satisfied, consumers are offered an opportunity to exchange them for their choice of a national brand.









To assure quality, our Pantry Pride products are laboratory-tested, kitchen-tested and taste-tested by consumers on a continuing basis, and reports are issued regularly as special bulletins so that consumers can test and compare ingredients more easily. Every Pantry Pride/Food Fair store has, in addition, a Taste-Test Book which shows results of all taste tests conducted comparing Pantry Pride products with national brand products.

The Company has voluntarily adopted the new uniform identity standards recommended by the National Live Stock and Meat Board, to eliminate consumer confusion in meat purchases. With more than 1,000 names in general use for only 300 separate retail meat cuts, many shoppers have not had a clear understanding of meat buying. The uniform meat labeling program offers a workable solution. The standards provide a system of uniform designations for retail cuts of beef, pork, lamb, veal and smoked meats, replacing the many local and regional designations.

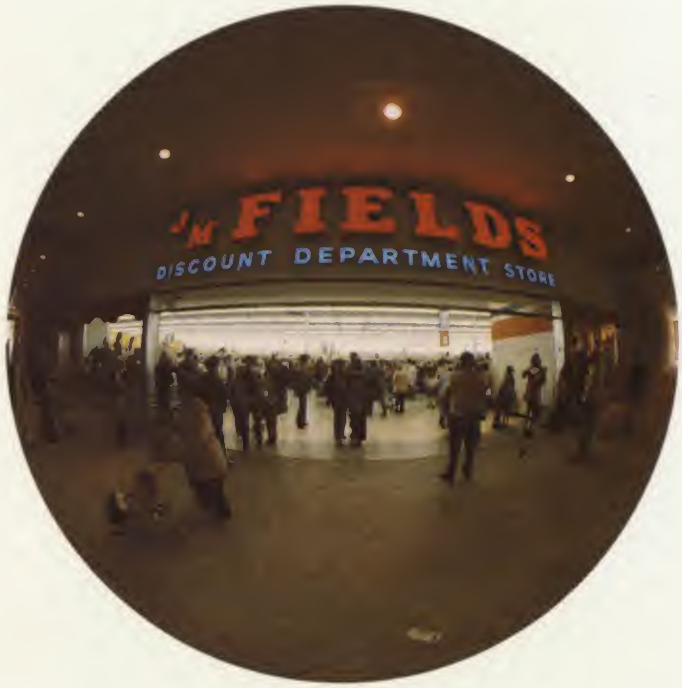
J. M. Fields has undertaken a number of programs to strongly identify its stores as ones in which consumers can shop with confidence, secure in the knowledge we stand behind every item we sell . . . that there is no question about our guarantee and refund policy.

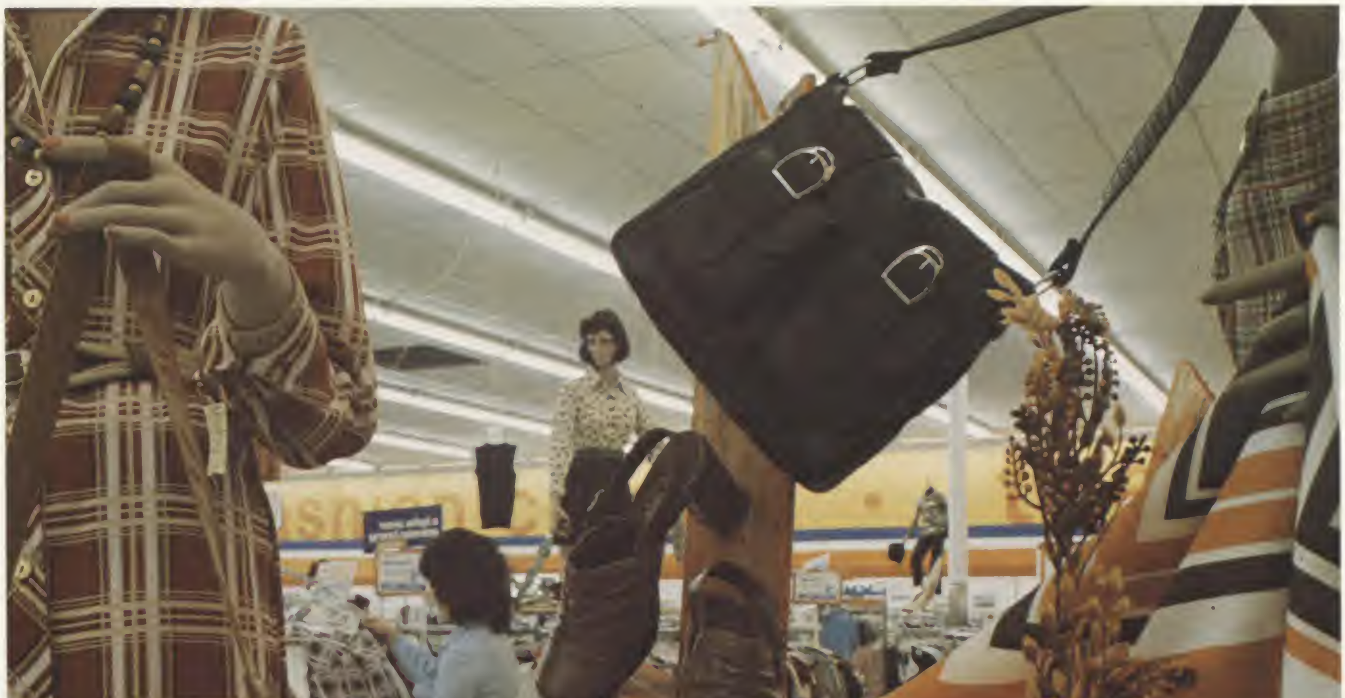
This has been done by stating clearly and forcefully: "Our guarantee has no fine print. If anything you purchase doesn't measure up to your expectations, let us know. We'll make every effort to correct what is wrong. If we can't, you'll get a full refund or adjustment . . . without a hassle. You must be satisfied. . . . " This statement is publicized in newspaper ads, circulars, radio, television and signwork throughout the stores.

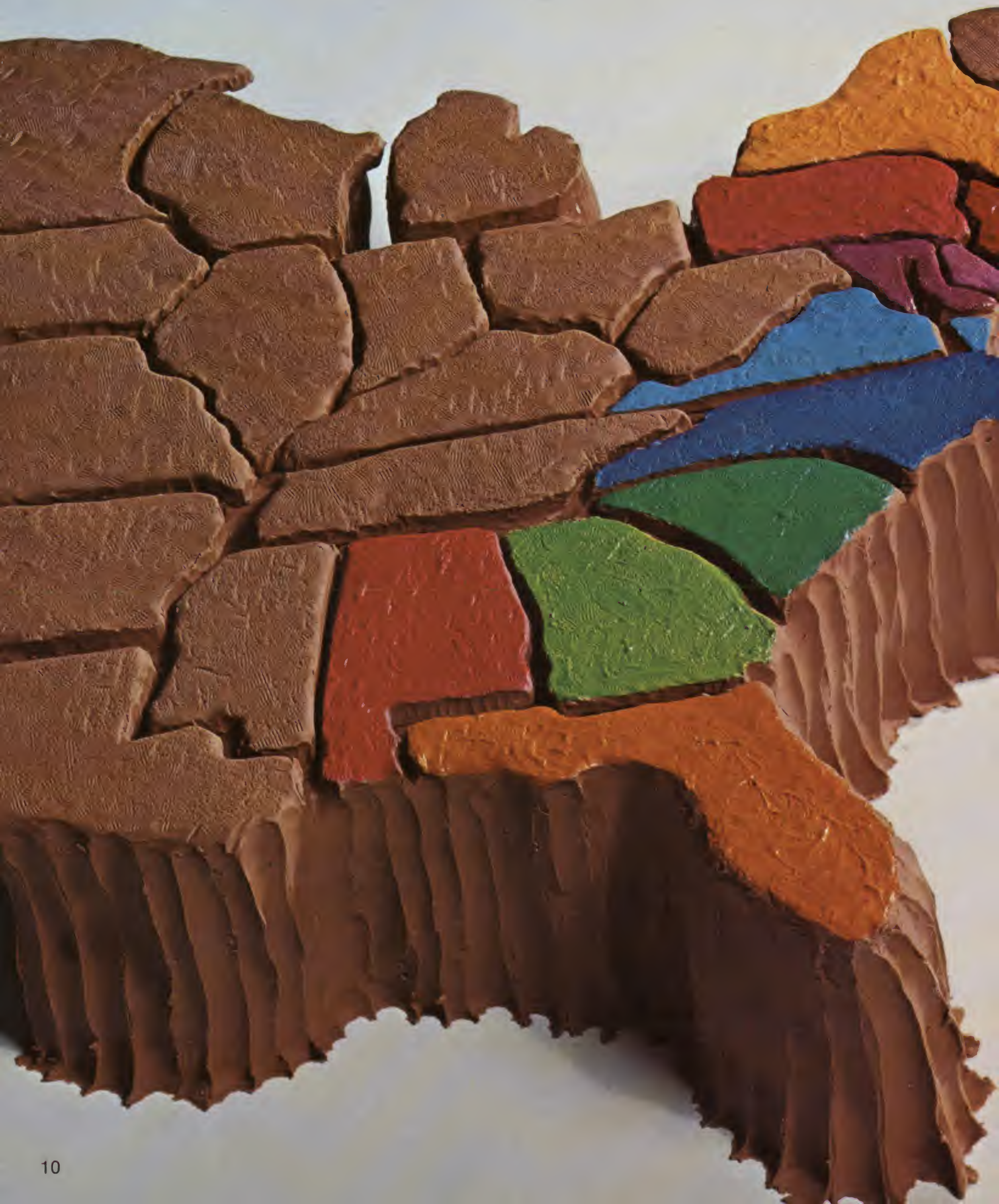
In addition, shoppers are given the opportunity to "sound off" by calling collect to J. M. Fields' consumer affairs office in New York with recommendations, comments or complaints.

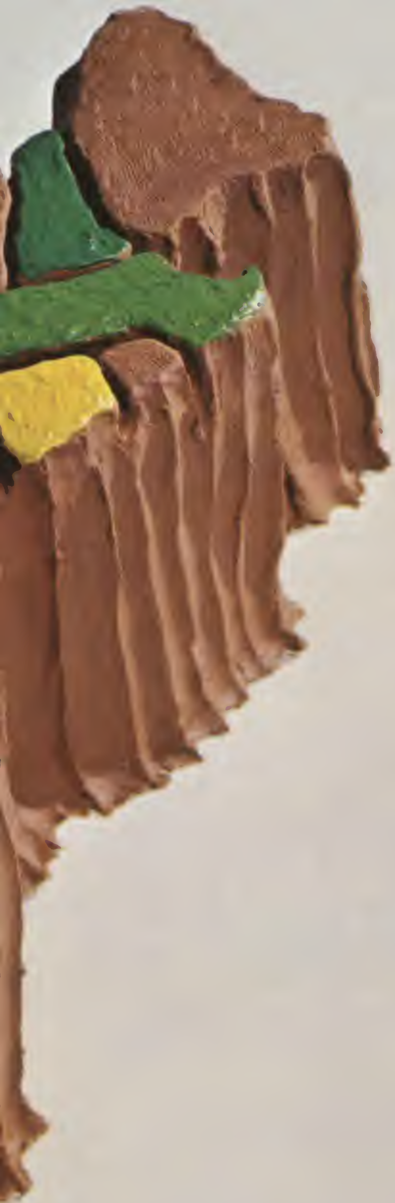
A pilot consumer board has been set up in the Rochester, N.Y., area where shoppers can express their views on broad-ranging subjects directly to management. Consumer boards in other areas are under consideration.

Another facet of this program is emphasis on quality control. Product testing against rigid quality standards has been expanded during the past year to all departments. Ready-to-wear merchandise is being subjected to higher standards in tests for color, fit and workmanship, and is pre-tested for quality before buyers consider placing the items in the stores. Soft goods lines are being upgraded for broader customer appeal while still maintaining an aggressive discount policy. A soft lines merchandise planning department has been established to speed responses to fashion needs at store level and assist in buying and distribution. Stores are being updated for more appeal to the fashion customer.





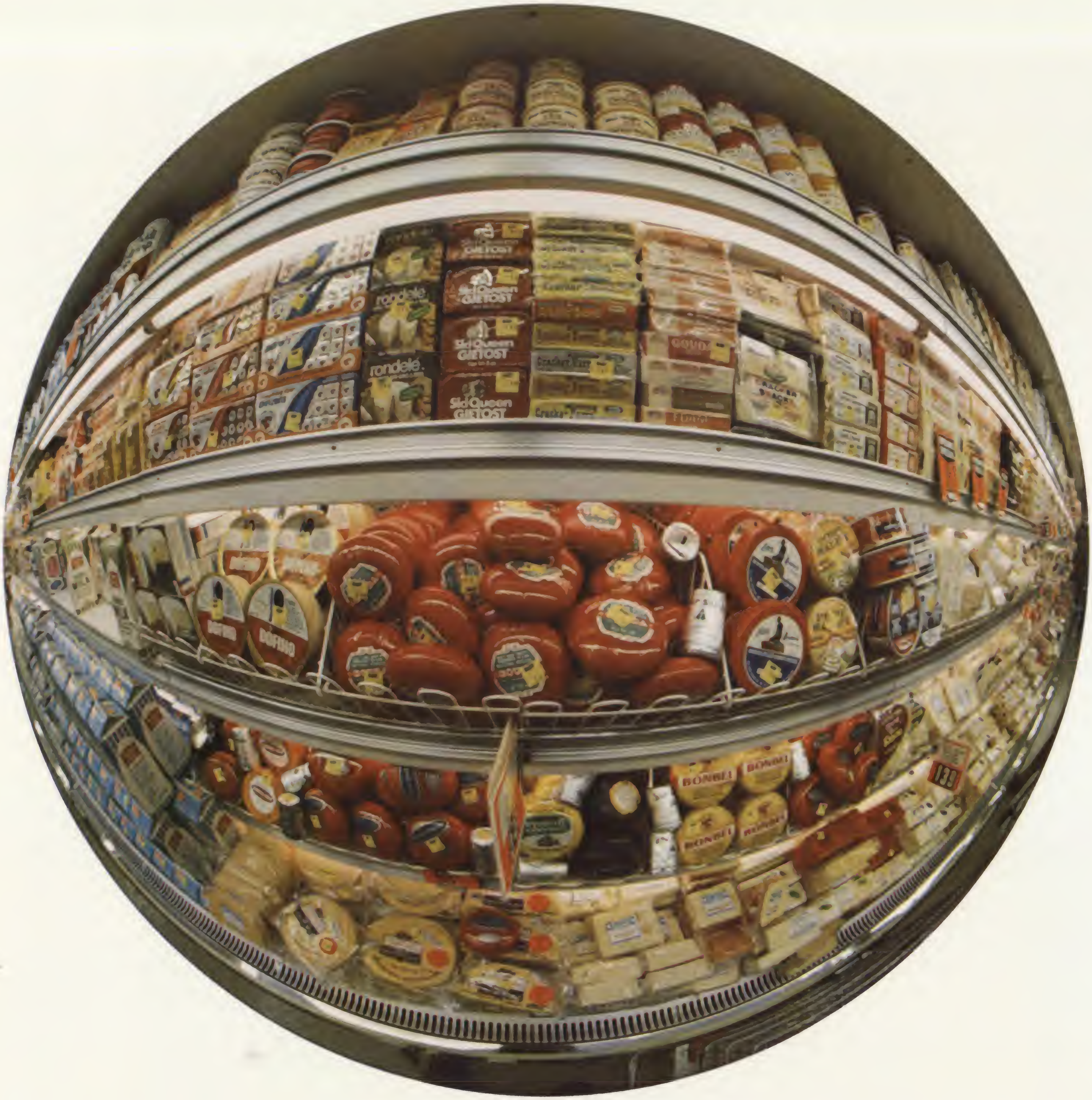




Food Fair Stores, Inc.

as of August 3, 1974

STATE	FOOD UNITS	DEPARTMENT STORES
Alabama	2	—
Connecticut	15	3
Delaware	7	—
Florida	167	35
Georgia	8	4
Maryland	47	—
Massachusetts	—	8
New Hampshire	—	5
New Jersey	62	9
New York	54	7
North Carolina	—	1
Pennsylvania	83	4
South Carolina	3	4
Virginia	22	5
TOTAL	470	85


rondelé
Ski Queen
GJETOST
BONBEL

Statistical Summary

Food Fair Stores, Inc. and Subsidiaries

(all dollar figures are in thousands, except per share amounts)	fiscal year 1974(a)	1973	1972	1971	1970
Sales	$2,380,561	$2,092,127	$1,980,458	$1,805,855	$1,649,790
Net income (loss):					
Continuing operations	$ 8,926	$ 6,162	$ 7,002	$ 13,916	$ 12,013
Discontinued operations			(5,451)	(3,066)	(1,213)
Income before extraordinary items	$ 8,926	$ 6,162	$ 1,551	$ 10,850	$ 10,800
Income per share of common stock before extraordinary items (b)	$ 1.18	$ .80	$ .19	$ 1.42	$ 1.42
Extraordinary items:					
Provision for losses relating to discontinued operations		($ 4,031)	($ 2,949)		
Tax benefit arising from net operating loss carryforward				$ 549	$ 167
Net income (loss)	$ 8,926	$ 2,131	($ 1,398)	$ 11,399	$ 10,967
Net income (loss) per share of common stock (b)	$ 1.18	$ .27	($ .20)	$ 1.49	$ 1.44
Cash dividends	$ 1,597	$ 1,608	$ 4,113	$ 6,658	$ 6,645
Earnings retained	$ 7,329	$ 523	($ 5,511)	$ 4,741	$ 4,322
Depreciation	$ 16,865	$ 17,125	$ 17,310	$ 15,814	$ 14,167
Current assets	$ 305,791	$ 258,306	$ 273,769	$ 260,470	$ 238,805
Current liabilities	$ 193,943	$ 145,462	$ 163,174	$ 132,831	$ 135,326
Shareholders' equity	$ 140,208	$ 133,738	$ 133,383	$ 138,914	$ 134,282

(a) 53 Weeks.
(b) Retroactive effect has been given to the 2% common stock dividends issued in 1973 and 1972.

Consolidated Balance Sheet

Food Fair Stores, Inc. and Subsidiaries

August 3, 1974 and July 28, 1973

Assets

	1974	1973
Current assets:		
Cash	**$ 25,700,000**	$ 24,168,000
Marketable securities	**530,000**	454,000
Funds held for retirement of bonds (Note 6)	**6,677,000**	
Accounts receivable, net of allowance for doubtful accounts, $880,000, 1974; $1,560,000, 1973	**22,830,000**	20,462,000
Inventories	**238,314,000**	199,768,000
Prepaid expenses	**10,457,000**	9,428,000
Real estate in the process of development and sale, net of payments received on account, $2,500,000	**300,000**	
Advances to Fields Credit Corp. (Note 4)	**983,000**	4,026,000
Total current assets	**305,791,000**	258,306,000
Investments (Notes 4 and 5):		
Fields Credit Corp.	**6,193,000**	6,022,000
Amterre Development Inc.	**9,444,000**	9,172,000
Other subsidiaries	**5,080,000**	4,337,000
Miscellaneous	**1,282,000**	1,299,000
	21,999,000	20,830,000
Property, plant and equipment:		
Land	**12,141,000**	11,520,000
Buildings and improvements	**56,232,000**	55,169,000
Fixtures and equipment	**141,502,000**	139,154,000
	209,875,000	205,843,000
Less accumulated depreciation	**93,824,000**	86,280,000
	116,051,000	119,563,000
Funds held for retirement of bonds (Note 6)		6,898,000
Other assets:		
Accounts and notes receivable, not current	**5,481,000**	5,885,000
Deferred charges	**4,845,000**	5,026,000
Miscellaneous	**3,583,000**	3,912,000
	13,909,000	14,823,000
	$457,750,000	$420,420,000

Liabilities and Shareholders' Equity

	1974	1973
Current liabilities:		
Notes payable (Note 7)	**$ 7,286,000**	$ 8,690,000
Current portion of long-term debt (Note 7)	**13,923,000**	3,699,000
Accounts payable	**128,389,000**	91,804,000
Accrued salaries and other expenses	**36,111,000**	35,703,000
Income taxes (Note 11)	**8,234,000**	5,566,000
Total current liabilities	**193,943,000**	145,462,000
Other liabilities:		
Long-term debt, net of current portion (Note 7)	**112,528,000**	129,962,000
Lease obligations for closed stores	**554,000**	1,917,000
Deferred income tax (Note 11)	**10,074,000**	8,776,000
Minority interest in subsidiaries	**443,000**	565,000
	123,599,000	141,220,000
Commitments and contingencies (Notes 11, 13 and 14)		
Shareholders' equity:		
Preferred stock (Note 8)	**2,177,000**	2,578,000
Common stock (Note 9)	**7,557,000**	7,557,000
Capital in excess of par (Note 10)	**51,125,000**	50,972,000
Retained earnings (Note 7)	**79,996,000**	72,667,000
	140,855,000	133,774,000
Less cost of common shares in treasury, 86,749, 1974; 3,300, 1973	**647,000**	36,000
	140,208,000	133,738,000
	$457,750,000	$420,420,000

See notes to consolidated financial statements.

Consolidated Statement of

Income

Food Fair Stores, Inc. and Subsidiaries

Years ended August 3, 1974 and July 28, 1973

	1974 (53 weeks)	1973 (52 weeks)
Income:		
Sales	$2,380,561,000	$2,092,127,000
Equity in earnings of unconsolidated subsidiaries	1,340,000	778,000
Other	3,955,000	1,828,000
	2,385,856,000	2,094,733,000
Costs and expenses:		
Cost of sales	1,916,737,000	1,699,929,000
Operating, general and administrative expenses	442,452,000	374,057,000
Interest	13,576,000	12,645,000
	2,372,765,000	2,086,631,000
Income before income taxes	13,091,000	8,102,000
Income taxes (Note 11)	4,165,000	1,940,000
Income before extraordinary item	8,926,000	6,162,000
Extraordinary item (Note 3)		(4,031,000)
Net income	$ 8,926,000	$ 2,131,000
Income per share of common stock:		
Income before extraordinary item	$ 1.18	$ .80
Extraordinary item		(.53)
Net income	$ 1.18	$ .27

Consolidated Statement of

Retained Earnings

Food Fair Stores, Inc. and Subsidiaries

Years ended August 3, 1974 and July 28, 1973

	1974 (53 weeks)	1973 (52 weeks)
Balance, beginning of year, as previously reported	$ 73,790,000	$ 74,786,000
Less adjustment relating to examination by Internal Revenue Service	1,123,000	1,123,000
Balance, beginning of year, restated	72,667,000	73,663,000
Add net income for the year	8,926,000	2,131,000
	81,593,000	75,794,000
Deduct dividends:		
Cash:		
Preferred stock	94,000	110,000
Common stock	1,503,000	1,498,000
2% common stock dividend		1,519,000
	1,597,000	3,127,000
Balance, end of year	$ 79,996,000	$ 72,667,000

See notes to consolidated financial statements.

Consolidated Statement of

Changes in Financial Position

Food Fair Stores, Inc. and Subsidiaries

Years ended August 3, 1974 and July 28, 1973

	1974 (53 weeks)	1973 (52 weeks)
Source of funds:		
Income before extraordinary item	**$ 8,926,000**	$ 6,162,000
Add (deduct) items not affecting working capital:		
Depreciation	**16,865,000**	17,125,000
Amortization	**291,000**	206,000
Deferred income taxes	**1,099,000**	575,000
Undistributed earnings of unconsolidated subsidiaries	**(1,340,000)**	(778,000)
Working capital provided from operations, exclusive of extraordinary item	**25,841,000**	23,290,000
Extraordinary item		(4,031,000)
Disposition of property, plant and equipment	**2,951,000**	2,613,000
Decrease in other assets	**623,000**	
Increase in:		
Long-term debt	**1,052,000**	41,276,000
Lease obligations for closed stores		1,917,000
Transfer of funds held for retirement of bonds to current assets	**6,898,000**	
	37,365,000	65,065,000
Application of funds:		
Purchase of property, plant and equipment	**16,304,000**	18,195,000
Decrease in:		
Long-term debt	**18,486,000**	27,835,000
Lease obligations for closed stores	**1,363,000**	
Payment of cash dividends	**1,597,000**	1,608,000
Funds held for retirement of bonds		6,898,000
Adjustment relating to examination by Internal Revenue Service		1,123,000
Increase in:		
Investments		5,436,000
Other assets		1,659,000
Other changes, net	**611,000**	1,185,000
	38,361,000	63,939,000
Increase (decrease) in working capital	**($ 996,000)**	$ 1,126,000
Summary of net changes in working capital:		
Increase (decrease) in current assets:		
Cash	**$ 1,532,000**	$ 7,854,000
Marketable securities	**76,000**	(13,000)
Funds held for retirement of bonds	**6,677,000**	
Accounts receivable	**2,368,000**	(48,136,000)
Inventories	**38,546,000**	27,893,000
Prepaid expenses	**1,029,000**	(329,000)
Real estate in the process of development and sale, net	**300,000**	(573,000)
Advances to Fields Credit Corp.	**(3,043,000)**	4,026,000
Income tax refunds receivable		(6,185,000)
	47,485,000	(15,463,000)
Increase (decrease) in current liabilities:		
Notes payable	**(1,404,000)**	(31,114,000)
Current portion of long-term debt	**10,224,000**	(639,000)
Accounts payable	**36,585,000**	14,960,000
Accrued salaries and other expenses	**408,000**	165,000
Income taxes	**2,668,000**	39,000
	48,481,000	(16,589,000)
Increase (decrease) in working capital	**($ 996,000)**	$ 1,126,000

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

1. Summary of significant accounting policies:

Basis of consolidation: The consolidated financial statements include the accounts of the Company and its wholly and majority owned subsidiaries, except the life insurance and credit companies. All significant intercompany balances and transactions have been eliminated. Intercompany profits, if any, in the inventories, are not significant.

Investments in the life insurance and credit companies, 50% owned companies and Amterre Development Inc. are stated at the Company's equity in net assets.

Marketable securities: Marketable securities are stated at cost.

Inventories: Inventories are stated at cost (first-in, first-out or average), which is market or lower. The retail method of accounting is used with respect to inventories of merchandise in stores.

Investments, miscellaneous: Miscellaneous investments are stated at cost.

Property, plant and equipment: Property, plant and equipment are stated at cost. Depreciation for financial reporting purposes is computed on the straight-line method over the estimated useful lives of the assets. For income tax reporting purposes, depreciation is computed by accelerated methods.

Provisions for credit losses and charge off policy: Provision for losses on customers' accounts arising from credit sales is made to maintain adequate reserves to cover anticipated losses. Customers' accounts are charged off against the reserve if no payment is received for a stipulated period, or if accounts become uncollectible for other reasons.

Income taxes: Income taxes are provided on all transactions included in the determination of financial income. Where such transactions are included in the determination of taxable income in a different year, such as the acceleration of depreciation and the deferral of gross profit on installment sales, the resulting tax benefits are deferred. Current investment tax credits are being taken into income as the related assets are placed in service.

Other: Debt expense is being amortized over the term of the debentures. If debentures are retired prior to maturity, the unamortized discount and expense is charged to operations.

The excess of cost over net assets of a business acquired in 1971 is being amortized over forty years.

Pre-opening expenses of J. M. Fields department stores are deferred and charged to operations over a three year period. With respect to food stores, losses incurred in the initial three months by new stores, remodeled stores, and stores converted to discount operations are deferred and amortized over a three year period.

Pension plans: Pension expense includes normal cost and amortization of prior service costs over a forty year period. The Company's policy is to fund pension costs accrued.

Income per share of common stock: Income per share of common stock is based on the weighted average number of shares outstanding during the years. Warrants and convertible subordinated notes have no dilutive effect.

2. Reclassification: The financial statements for fiscal 1973 have been reclassified to conform with the presentation for 1974.

3. Extraordinary item: The extraordinary item in 1973 represents additional losses, net of applicable income taxes, relating to the termination of the West Coast supermarket operations in 1972.

4. Investment, Fields Credit Corp.: Fields Credit Corp. commenced operations on July 25, 1973 and purchased the revolving credit and installment sales accounts of J.M. Fields, Inc. subject to the related unearned income and the allowance for doubtful accounts. The accounts transferred to Fields Credit Corp. are with recourse to J. M. Fields, Inc. and Food Fair Stores, Inc. Pretax earnings of $353,725 in 1974 and $44,525 in 1973, have been included in the consolidated statement of income as a reduction of interest expense. The balance sheet of Fields Credit Corp. at August 3, 1974 and July 28, 1973 is as follows:

	1974	1973
Assets	(000's omitted)	
Cash	$ 82	
Due from J. M. Fields, Inc.	550	
Customers' receivables	35,745	$32,736
Unearned income	(1,248)	(1,195)
Allowance for doubtful accounts	(517)	(474)
	$34,612	$31,067
Liabilities and Equity		
Notes payable, banks	$27,000	$21,000
Advances from Food Fair Stores, Inc.	983	4,026
Accrued expenses	436	19
Subordinated notes payable to Food Fair Stores, Inc.	5,900	5,900
Equity of Food Fair Stores, Inc.	293	122
	$34,612	$31,067

5. Investment, Amterre Development Inc.: The Company owns all of the preferred stock and 40% of the common stock of Amterre Development Inc. At August 3, 1974, the value of the preferred stock was $2,000,000 and the market value of the common stock was $3,333,333 based on a quoted bid price of $1 per share.

Net earnings of Amterre Development Inc. included in the consolidated statement of income is $242,000 ($.03 per share) in 1974 and $235,000 ($.03 per share) in 1973.

Condensed financial statements of Amterre Development Inc. and subsidiaries are as follows:

5. Investment, Amterre Development Inc. (Continued):

Consolidated balance sheet:	December 31, 1973	1972
	(000's omitted except per share amounts)	
Assets		
Investment in property and equipment, at cost, net of accumulated depreciation	$240,851	$234,451
Other	10,097	9,911
	$250,948	$244,362
Liabilities		
Notes, mortgages and debentures payable	$212,832	$201,617
Construction loans payable	4,900	7,431
Other	12,602	15,382
	230,334	224,430
Shareholders' equity	20,614	19,932
	$250,948	$244,362

Consolidated statement of income:	Year ended December 31, 1973	1972
Income	$ 34,179	$ 30,418
Expenses, net	33,055	29,510
Income before income taxes	1,124	908
Income taxes	351	154
Net income	$ 773	$ 754
Earnings per common share and common share equivalent	$.08	$.08

With respect to other financial information, reference is made to the published financial statements and related footnotes in the annual report of Amterre Development Inc. for 1973.

6. Funds held for retirement of bonds: This amount represents certificates of deposit held by the trustee for the redemption of the 3⅜% sinking fund debentures, retired on September 1, 1974.

7. Indebtedness:

	Rate	Amount (000's omitted)	Maturity
Notes:			
Banks	7 to 13.9%	$ 26,007	1974-1980
Other	6%-8.75%	7,455	1974-1984
Mortgages	5%-10%	11,950	1974-1998
Sinking fund debentures	3.375%	6,536	1974
Convertible subordinated notes	4%	1,440	1977
Subordinated debentures	4%	13,063	1979
Subordinated notes	8.5%	25,000	1984
Sinking fund debentures	8.375%	35,000	1996
		126,451	
Less current portion		13,923	
		$112,528	

Sinking fund debentures (3.375%) were retired on September 1, 1974.

Convertible subordinated notes (4%) are convertible into common stock at $25 per share through May 12, 1977. These notes require annual principal payments of $480,000.

Subordinated debentures (4%) require annual sinking fund payments of $967,000. The sinking fund requirements for the year ending August 2, 1975 have been anticipated.

Subordinated notes (8.5%) require annual payments of $2,000,000 beginning December 1, 1974.

Sinking fund debentures (8.375%) require annual sinking fund payments of $1,750,000 commencing January 15, 1977.

The indentures covering the issuance of the debentures and notes described above contain restrictions as to the payment of cash dividends and the redemption of shares of stock of the Company. The maximum amount of retained earnings so restricted at August 3, 1974 was $60,847,000.

At August 3, 1974, the Company had lines of credit available from various banks in the amount of $102,170,000 at the prevailing prime interest rate. These lines are supported by the Company's normal cash balances maintained on a daily basis and there is no legal restriction on the availability of such balances. During fiscal 1974, short-term borrowings averaged approximately $18,700,000 (maximum $31,900,000) at an average interest rate of 10.4%.

8. Preferred stock: Preferred stock is $4.20 cumulative, $15 par (stated at liquidating value of $100 per share); 108,190 shares are authorized, of which 21,768 are issued and outstanding. The Company is obligated to set aside $120,000 semi-annually as a sinking fund for the redemption of the preferred stock, which may be called for this purpose at $100 per share plus accrued dividends.

9. Common stock: Common stock is $1 par; 10,000,000 shares are authorized, of which 7,557,378 are issued, 86,749 are held in the Company's treasury and 7,470,629 are outstanding.

At August 3, 1974, warrants to purchase 400,000 shares of common stock were outstanding. These warrants are exercisable at $23.05 per share and expire December 17, 1979.

10. Capital in excess of par: The increase in capital in excess of par during the year ended August 3, 1974 represents the excess of stated value over cost of cumulative preferred stock retired.

11. Income taxes: The provision for income taxes aggregated $4,165,000 in 1974 and $1,940,000 in 1973. An analysis of the provision is shown below:

	1974	1973
Federal:		
Current	$4,067,000	
Deferred	1,099,000	$2,896,000
Investment tax credit	(2,541,000)	(1,307,000)
State	1,540,000	351,000
	$4,165,000	$1,940,000

For the fiscal year 1974, the financial income subject to tax includes approximately $1,350,000 taxable at the capital gains rate.

The Company and its subsidiaries file a consolidated Federal income tax return. Investment tax credit carryforwards of approximately $3,000,000 are available for Federal income tax purposes for fiscal years ending after August 3, 1974, and expire through 1981.

The Federal income tax returns of the Company and certain subsidiaries have been examined by Internal

11. Income Taxes (Continued):

Revenue Service for the fiscal years 1964 through 1968. The Service has proposed adjustments which would result in additional taxes of approximately $9,200,000. The proposed adjustments are being contested by the Company. In the opinion of management, based upon the advice of tax counsel, the final net additional tax will be substantially less than the amounts proposed.

12. Pension plans: The Company and its subsidiaries have several noncontributory pension plans covering certain hourly and salaried employees. Pension expense for the years ended August 3, 1974 and July 28, 1973 was $1,135,000 and $1,191,000, respectively. The total assets of the plans exceeded the actuarially computed value of vested benefits.

13. Contingencies: The Company and Amterre Development Inc. have been named as defendants in a complaint issued by the Federal Trade Commission alleging that Amterre is a "subsidiary" and is controlled by the Company, and that the Company and Amterre, through restrictive provisions in shopping center leases, have entered into agreements which tend to fix prices and restrain trade. The Company and Amterre have filed answers which deny the material allegations of the complaint. The complaint does not seek money damages and, in the opinion of management, if the relief sought by the Federal Trade Commission is granted, such result will not have a material adverse effect upon the financial position of the Company.

The Company is contingently liable at August 3, 1974 for accounts receivable aggregating $7,870,000 sold to a bank with recourse.

On September 2, 1974, the Congress enacted the Pension Reform Act of 1974. Major provisions of the new legislation relate to participation, vesting and funding requirements. The impact of the requirements of the Act on the financial statements of the Company cannot be determined until actuarial studies now in progress are completed. In the opinion of management, any increase in funding resulting from the studies will not have a material effect on the financial position of the Company.

14. Leases: At August 3, 1974, the Company was lessee under leases covering principally retail locations and distribution centers. Realty lease terms generally range to twenty-five years, with options of renewal for additional periods. Equipment leases expire at various dates through 1984.

The Company has classified its lease obligations as either noncapitalized financing leases or other leases in accordance with the requirements of the Securities and Exchange Commission. Rental expense for the fiscal years 1974 and 1973 was as follows:

	1974	1973
	(000's omitted)	
Financing leases:		
Minimum rentals	$21,387	$19,216
Contingent rentals	406	228
Sublease rentals	(1,857)	(1,569)
	19,936	17,875
Other leases:		
Minimum rentals	14,855	15,325
Contingent rentals	1,440	808
Sublease rentals	(576)	(541)
	15,719	15,592
	$35,655	$33,467

Minimum rental commitments, exclusive of taxes and other costs paid by the Company, for noncancellable leases in effect at August 3, 1974 are approximately as follows for the periods indicated:

Fiscal year	Minimum rental commitments: Financing leases	Minimum rental commitments: Other leases	Minimum rentals from subleases	Net commitments
	(000's omitted)			
1975	$ 20,139	$13,455	$ 2,331	$ 31,263
1976	20,367	12,585	1,956	30,996
1977	20,604	11,858	1,665	30,797
1978	20,590	11,166	1,497	30,259
1979	20,667	10,281	1,333	29,615
1980–1984	18,406	7,794	1,114	25,086
1985–1989	13,638	4,037	404	17,271
1990–1994	9,485	1,455	248	10,692
Thereafter	8,113	144	238	8,019
	$152,009	$72,775	$10,786	$213,998

The present value of minimum rental commitments for noncapitalized financing leases was $185,135,000 at August 3, 1974 and $186,302,000 at July 28, 1973, based on calculations using interest rates ranging from 4.25% to 10%. The weighted average interest rates were 6.9% and 6.8% for 1974 and 1973, respectively.

If, instead of recording rental expense, all financing leases were capitalized, related assets were amortized on a straight-line basis and interest costs were accrued on the basis of outstanding lease liability, the effect on net income would be a reduction of $1,448,000 in 1974 and $2,070,000 in 1973. The amounts of amortization and interest included in the calculations were as follows:

	1974	1973
Amortization	$ 9,499,000	$ 8,547,000
Interest cost	12,919,000	11,838,000

The Board of Directors and Shareholders
Food Fair Stores, Inc.

We have examined the consolidated balance sheet of Food Fair Stores, Inc. and Subsidiaries as at August 3, 1974 and July 28, 1973 and the related consolidated statements of income, retained earnings and changes in financial position for the fifty-three and fifty-two weeks, respectively, then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, subject to the outcome of the tax matter described in Note 11, the financial statements referred to above present fairly the financial position of Food Fair Stores, Inc. and Subsidiaries at August 3, 1974 and July 28, 1973, the results of their operations and changes in financial position for the respective fifty-three and fifty-two weeks then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Laventhol Krekstein Horwath & Horwath

Philadelphia, Pa.
October 16, 1974

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Chief Executive Officer

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Assistant Secretary

Edmond O'Neill
Assistant Secretary

Harvey Richards
Assistant Secretary

Leonard Stubins
Assistant Secretary

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First Pennsylvania Bank

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MGS Incentives Company

Harold H. Rubin
President

Washington Square Life Insurance Co.

E. Ernest Johnson
Vice President

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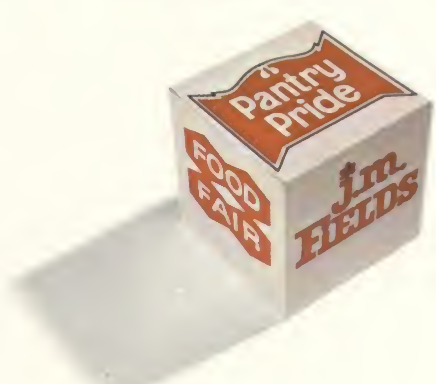
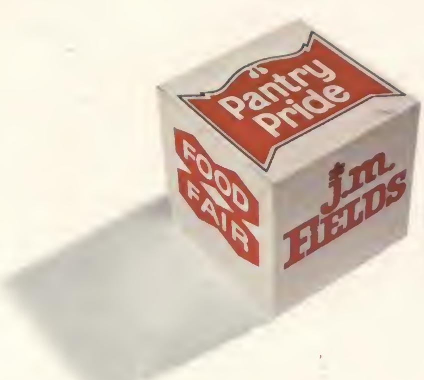
General Counsel Stein & Rosen, New York, New York
Transfer Agent Registrar & Transfer Company, New York, New York
Registrar The Chase Manhattan Bank N.A., New York, New York
Certified Public Accountants Laventhol Krekstein Horwath & Horwath, Philadelphia, Penna.

Annual Meeting The annual meeting of shareholders will be held Tuesday, November 19, 1974, at 2 P.M., local time, in the Bellevue Stratford Hotel, Broad and Walnut Sts., Philadelphia. Shareholders are cordially invited to attend.





FOOD FAIR STORES, INC.

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